

October 1955

ECONOMIC SITUATION IN TAIWAN

1. General. During the past year the stability of the Taiwan economy has been threatened, despite a sharp increase in US aid other than MDAP supplies, owing to a temporary setback in the expansion of production and to a sharp increase in budgetary expenditures for military and social welfare purposes without a corresponding expansion of revenues. Although the productive capacity of the island has increased satisfactorily, a severe drought in the winter and spring of 1954-55 has reduced current output. At the same time, the Communist military threat and the receipt of MDAP supplies has led to a sharp increase in military expenditures as well as in related expenditures for the resettlement of refugees from the Tachen Islands and of discharged servicemen. The Chinese authorities have refused to risk popular disaffection through a commensurate increase in revenues, and, in budgeting for a very large deficit, have ignored the fiscal advice of US aid officials on Taiwan, apparently in the expectation that deteriorating economic conditions will force the US to extend greater economic aid to Taiwan.

2. Level of production. Agricultural production in 1955 is expected to decline one percent from 1954 levels as a result of a severe spring drought which reduced the first rice crop by nearly one-fifth and also affected the output of tea, citrus fruits, peanuts, and next year's sugar cane crop. However, there was satisfactory progress in agricultural development programs. This year's sugar cane crop as compared with last year's produced nearly 5 percent more sugar from nearly 20 percent less planted acreage, due in part to good weather but also to the development of high-yield strains and other technical improvements. Water conservancy, pest and disease control programs, the development of special crops, and other agricultural programs have continued, and are expected to increase the productivity of Taiwan agriculture over the next few years by an annual average of over one percent.

Industrial output, while expected to rise in 1955, was adversely affected in the first half of the year by the drought which reduced hydro-electric power generation and curtailed industrial operations, particularly in the aluminum and fertilizer industries. Restrictions on raw material imports, forced by foreign exchange shortages, have also had some adverse effect on industrial productivity. Despite these factors, a high internal demand and the expansion of power generating capacity is expected to sustain a continuing expansion of industrial output, although not at the 9 percent rate achieved in 1954. Completion of current projects will increase generating capacity by 134,000 KW or by one-third during 1955, which increase is expected to reduce the power shortages that have hampered industrial output for the past several years and permit a substantial increase in industrial output in 1956.

25 YEAR
RE-REVIEW

ECONOMIC INDICATORS

	1938	1951	1952	1953	1954	1955
Agricultural production (1938 = 100)	100	83	101	98	97	96 (prelim. estimate)
Industrial production (1941 = 100)	(1937) 79	92	111	140	152	(Jan-Mar. seasonally adjusted) 158
GNP (1954 dollars)		1,050	1,235	1,345	1,480	
Per capita GNP (dollars)		115	130	136	146	
Wholesale prices (1952 = 100)		82	100	109	111	123 (July)

3. Fiscal developments. Taiwan's fiscal situation has been marked by sharply rising military and social welfare expenditures. Military expenditures have risen owing to actions taken to counter the Communist military threat and to the construction, training, and other expenditures involved in the arrival and deployment of MDAP supplies. Special expenditures have arisen in the program to resettle the refugees from the Tachen Island group as well as the discharged servicemen. In consequence, total central and provincial government expenditures increased from US \$240 million in fiscal 1954 to \$284 million in fiscal 1955, and are budgeted at \$342 million in fiscal 1956.

The Chinese government has been reluctant to take measures to increase revenues from domestic sources for fear of alienating popular support, and in consequence the budget deficit has increased from \$55 million and \$68 million in fiscal 1954 and 1955 to \$120 million in the 1956 fiscal budget. Budget support from counterpart funds covered the deficit in fiscal 1954 and 1955, but US aid officials have insisted that counterpart budgetary support should not be increased in fiscal 1956 but that the deficit should be reduced on the basis of specific fiscal recommendations. Thus far, the Chinese officials have ignored the US advice and apparently expect that with the expansion of inflationary pressures the US will extend additional aid to stabilize the Taiwan economy.

CONSOLIDATED STATEMENT OF NATIONAL AND PROVINCIAL GOVERNMENT
FINANCES, 1952 - BUDGET 1956
(In million US dollars)

	Fiscal year ending Dec 31		Fiscal year ending June 30		
	1952	1953	1954	Budget 1955	Budget ^a 1956
<u>Expenditures</u>	<u>172.8</u>	<u>210.8</u>	<u>240.0</u>	<u>283.8</u>	<u>341.7</u>
National defense	99.3	122.1	156.0	189.0	213.0
Capital outlay	19.8	27.6	21.0	26.0	24.0
Grants and shared taxes to regional and local gov- ernments	16.2	11.0	11.8	12.4	11.1
Subsidies, interest, and other current costs	37.5	50.1	51.2	56.4	93.6
<u>Revenues from domestic sources</u>	<u>126.7</u>	<u>158.7</u>	<u>184.7</u>	<u>215.8</u>	<u>221.7</u>
Import and export taxes)	101.4	32.3	48.2	68.5	70.2
Other taxes and monopoly)		89.5	97.4	120.7	129.0
profits					
Profits of government enterprises	7.9	13.7	15.4	13.2	14.3
Profits from sale of foreign exchange	—	—	4.7	3.1	—
Other revenues	17.4	23.2	19.0	10.3	8.2
<u>Deficit exclusive of ICA counterpart</u>	<u>46.1</u>	<u>52.1</u>	<u>55.3</u>	<u>68.0</u>	<u>120.0</u>
<u>ICA counterpart released</u>	<u>38.6</u>	<u>50.9</u>	<u>53.0</u>	<u>67.0</u>	<u>n a</u>
Budgetary	17.8	12.2	10.0	22.0	<u>n a</u>
Extrabudgetary	20.8	38.7	43.0	45.0	<u>n a</u>
<u>Deficit inclusive of ICA counterpart</u>	<u>7.5</u>	<u>1.2</u>	<u>2.3</u>	<u>1.0</u>	<u>n a</u>

a. The proposed budget is being reappraised and it is hoped that a smaller deficit can be achieved.

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4. External accounts and US aid. Taiwan's balance of payments deteriorated in 1954 as exports declined by one-quarter while imports increased. In 1955, stricter controls were imposed over imports and increases in official exchange rates were made in an attempt to bring the external accounts into balance. Exports in 1955 are expected to increase with the allocation of large quantities of rice for export in addition to normal sugar exports. With the allotment of supplementary US aid in March 1955, aid-financed imports can be expected to increase by the end of the year and permit a reduction in the stringency of import controls.

US aid other than MDAP supplies was increased by over one-half in fiscal 1955 to a level of \$137 million, owing to the allocation of supplementary aid of \$48 million in March 1955, largely in support of the retired servicemen's program. This additional aid will provide increased imports toward the end of 1955 and thereby ease the current balance of payments difficulties. Although the counterpart proceeds of these additional aid-financed imports are earmarked for specific programs, the lag between their generation and their expenditure will have certain deflationary effects which may to some extent offset the inflationary impact of the large budgetary deficit.

TAIWAN'S EXTERNAL ACCOUNTS
(In million US dollars)

	1938	1951	1952	1953	1954	Jan-June 1955
Exports	130	93	120	130	98	63
Imports	104	151	222	199	205	90
Trade Balance	26	-58	-102	-69	-107	-27
Balance on current account of goods and services	<u>n a</u>	-61	-99	-80	-125	<u>n a</u>
Increase in official foreign exchange reserves (Decrease (-))	<u>n a</u>	10	4	16	-23	<u>n a</u>

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